

18 August 2016

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Cross Submission
Input Methodologies Review – draft decisions
Topic 7: Related Party Transactions

Asplundh welcomes the opportunity to provide a cross-submission on the submissions made by participants in respect of the Commerce Commission's ("the Commission") draft decisions on the *Input Methodologies* review (released on 16 June 2016).

Our cross-submission specifically relates to *Topic Paper 7: Related Party Transactions ("RPTs")*, with specific focus on how Electricity Distribution Businesses ("EDBs") procure competitive services for Network Vegetation Management Services.

We acknowledge that the regulatory framework for EDBs in NZ is complex, and we do not purport to be subject matter experts in the Input Methodologies or Information Disclosure. Our submission is made based on first principles and our experiences within the electricity network industry.

Cross-Submission

Asplundh fully supports the Commission's proposed next steps to further investigate the matter relevant to the related party transaction regime, including:

- *"The commercial rationale for ownership structures or joint ventures structures..."*
- *"The Types of ownership structures..."*
- *"The Terms of the contracts..."*
- *"The mix of business being undertaken..."*
- *"Why suppliers use certain related party options..."*

We welcome this as a step towards enabling greater transparency and ensuring fair market competition occurs for delivering skilled network vegetation risk reduction and management services, including utility arborist services.

Our submission focusses on two areas commented on by other participants, which we have grouped below.

(1) COMPETITIVE PROCUREMENT PROCESSES

From our experience there is a range of approaches being adopted by EDBs for procuring network vegetation management services – ranging from in-house, to restricted (invitation) tenders and lastly to open market tender processes.

Several general comments made by participants are highlighted below, with our cross-submission following:

ENA (s3)

“The objective should be to provide for the fair recovery of costs, at arms-length prices, with consistency between EDBs and transactions based on evidence”

PWC (s298)

“As related parties established by distributors will generally have some synergies with the distribution business it is not surprising that related parties and distributors would transact”

Aurora (s13)

“... a fundamental objective of the related party valuations provisions... is the recovery of efficient expenditure at prices that would be observed in an arms-length transaction, in a workable competitive market”

Orion (s98)

“The long term customer benefits are:

- *Lower Prices as a result of an efficient competitive tender process. Our policy is to grant contracts to the lowest conforming price tenders*
- *Ensures there is a provider with sufficient scale to meet our requirements particularly in emergencies”*

Cross-Submission

Where service providers are not invited to participate in a competitive process, they have no transparency of how efficient, or arms-length the services obtained by EDBs are from their in-house providers. However, our experience from working with EDBs and our understanding of the rates being charged to them by related parties, has shown that there can often be significant cost efficiencies available by using external providers.

We support the Commission further investigating the evidence that EDBs have efficient procurement processes, and that these processes obtain the outcomes/objectives of the Commission.

The selection of related parties can also impact on the availability of a *workable competitive market* for the network and community region that the EDB provides services to. Utilising in-house providers, or utilising a restricted process, can:

- Limit the skilled utility arborist market resources available to the EDB and external tree owner customers who need these services to meet current regulatory obligations;
- Limit the competitive nature of the market and pricing – impacting the efficiency of expenditure by EDBs and cost affordability for to customers;
- Limit access to global industry leading mechanical vegetation management equipment that often enables more productive operations at lower overall cost and increased safety;

- Pose barriers to entry/competition for other participants, which inhibits the ability for EDBs to obtain truly arms-length pricing and services.

For example:

- **Aurora** utilises their in-house provider Delta to deliver their vegetation management services. Asplundh have a local depot and provide utility vegetation clearance services to the Dunedin City Council, yet have not been invited to provide competitive pricing to Aurora.
- **Orion** utilise a restricted pricing process, inviting only 3 local preferred contractors to submit pricing, for a single year of works on selected feeders.

In respect of both of these examples we would challenge if this is a true competitive market process, delivering reasonable cost and value for money.

(2) DRIVERS & BENEFITS OF IN-HOUSE PROVIDERS

We acknowledge that EDBs operations are complex, require value to be achieved for their stakeholders, and that using external parties requires the capability to establish and manage contracting arrangements.

ENA (Section 2 Submission Summary) *“The Commission should be careful when considering related party trends to understand the underlying drivers, which may include business strategies, bringing contracting activities in-house, and the application of the 2012 IDD”*

Aurora (s13) *“There are a range of reasons why EDBs would prefer to procure these services from a related party particularly in regional areas, including more control over safety performance...and over the availability of skilled resources.”*

Cross Submission

Utilising external providers can deliver the same (or higher) levels of service and safety than using in-house providers. Establishing clear and defined service arrangements, supported by the recent H&S legislation amendments, ensures that competent service providers can and will manage safety in their operations.

Securing and developing skilled resource is a common issue, with arborist being a skill shortage industry. NZ currently has a competitive market for arborists, and Asplundh is investing in people through apprenticeship schemes to combat this. Where EDBs limit the contestable market (through the use of in-house providers), this can hinder the development of skilled resource for that market.

Thank you for the opportunity to make this submission. We support the Commission proposed next steps, and are happy to provide further input during this process. If you have any questions please contact me.



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